BRITISH COLUMBIA RAILWAY COMPANY

ANNUAL SERVICE PLAN

2005 – 2007

Honourable Kevin Falcon
Minister of Transportation, and
Minister Responsible for the British Columbia Railway Company

On behalf of the Board of Directors of the British Columbia Railway Company (BCRC), I am pleased to provide our Annual Service Plan 2005 to 2007.

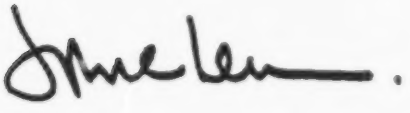
The last annual service plan prepared by BCRC was in fiscal 2003. In 2004, BCRC received an exemption from having to prepare a service plan because at that time, it was undergoing significant organizational transition and corporate restructuring.

The original mandate of BCRC was to construct and operate a freight railway in British Columbia. With the disposition of its shares in BC Rail Ltd. and its partnership interests in BC Rail Partnership to the Canadian National Railway Company (CN) thereby transferring the freight railway operations, the mandate of BCRC changed significantly. Residual assets and entities which continue to be owned and operated by BCRC and its subsidiaries, with the exception of the railway right-of-way, railbed and track infrastructure now leased to CN, are being disposed of according to the instruction of the Shareholder.

This Service Plan establishes a framework to guide: a) the development of appropriate accountability measures for BCRC's long-term mandate as landowner of the railway right-of-way, railbed and track; and b) the disposition of BCRC's remaining business units, assets and non-railway related real estate.

The British Columbia Railway Company Annual Service Plan 2005 to 2007, was prepared under the direction of the Board of Directors in accordance with the *Budget Transparency and Accountability Act*. The Plan is consistent with government's strategic priorities and overall strategic plan. All significant assumptions, policy decisions, and identifiable risks as of January 27, 2005, have been considered in preparing the Plan.

I am accountable for ensuring BCRC achieves the goals identified in the plan and for measuring and reporting performance.



John McLernon, Chair
British Columbia Railway Company

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1.0 ORGANIZATIONAL OVERVIEW

Enabling Legislation

The British Columbia Railway Company (BCRC) is a Crown corporation governed by two principal pieces of legislation. The *British Columbia Railway Act* establishes the corporation's structure, responsibilities and accountabilities. The *British Columbia Railway Finance Act* establishes the borrowing and investment framework for BCRC. BCRC must also meet the requirements of the *Financial Administration Act* and the *Budget Transparency and Accountability Act*.

Key Changes from Previous Service Plan

The last annual service plan prepared by BCRC was in fiscal 2003. In 2004, BCRC received an exemption from Section 13 (service plans for ministries and government organizations) of the *Budget Transparency and Accountability Act* because at that time, it was undergoing significant organizational transition and corporate restructuring. In July 2004, the BC Rail/Canadian National Railway Company (CN) Investment Partnership concluded and all of the freight railway operations of BCRC have since been assumed by CN. The remaining core business areas of and services provided by BCRC are described below.

Mandate

BCRC's original mandate was to construct and operate a freight railway in British Columbia. In July 2004, BCRC disposed of its shares in BC Rail Ltd. and its partnership interests in BC Rail Partnership to CN, the private sector operator selected to assume the freight railway operations. The residual assets and entities currently owned and operated by BCRC and its subsidiaries, with the exception of the railway right-of-way, railbed and track infrastructure now leased to CN for railway purposes, are not required to be publicly owned. As a result, the Shareholder has instructed the Board of Directors to continue to wind down or dispose of the remaining business units, assets and non-railway related real estate owned by BCRC and/or its subsidiaries.

Over the long-term, BCRC will continue to own the railway right-of-way, railbed and track infrastructure that supports the railway. In addition, as landowner, BCRC will have on-going accountability to oversee the Revitalization Agreement (lease agreement) with CN.

Core Business Areas and Services

BCRC is a commercial Crown corporation with all of its business activities operating in competition with the private sector. BCRC operates without government subsidies. Borrowing is done through the Ministry of Finance and full financial reporting is

provided according to the provisions of the *Budget Transparency and Accountability Act*.

BCRC has several operating subsidiaries, including:

BCR Port Subdivision Ltd.
~ This subsidiary operates the 23 mile railway line connecting three major railways (CN, Canadian Pacific Railway and Burlington Northern Santa Fe) with the port terminals at Roberts Bank. While operating none of its own trains on this railway line, the BCR Port Subdivision maintains the track and manages the operations on a shared cost basis of its users.

BCR Properties Ltd.
~ This subsidiary owns and manages all of the real estate not required to support railway operations. The portfolio consists of approximately 395 parcels of commercial, industrial and vacant land.

BCR Captive Insurance Co. Ltd.
~ This wholly owned insurance company provides primary property, general liability, terminal operator's liability, automobile physical damage and excess automobile liability coverage to BCRC and any subsidiary in which BCRC has a controlling interest. BCR Captive is regulated by the Financial Institutions Commission, and co-managed by BCRC and Aon Insurance Managers.

Vancouver Wharves Ltd.
~ Based in North Vancouver, this port facility handles inbound and outbound shipments of mineral concentrates, pulp, sulphur, fertilizers and agri-products.

In addition, there are other non-operational subsidiaries, many of which are currently in the process of being wound down and/or dissolved.

Governance

BCRC's seven-member Board of Directors, appointed by the Province, reports to the Minister of Transportation. The Board is responsible for overseeing the conduct of BCRC's business, directing management and ensuring that all major issues affecting the business affairs of BCRC are given appropriate consideration. The Board delegates responsibility for the day-to-day leadership and management of BCRC to its President and Chief Executive Officer.

The Board functions though a series of committees appointed to deal with specific matters. These Committees generally meet quarterly in conjunction with full Board meetings.

There are currently three standing committees of the Board:

Audit, Finance and Risk Management Committee
~ Assists the Board of Directors in fulfilling its obligations and oversight responsibilities relating to the audit process, financial reporting, the system of corporate controls, governance of financial investments and various aspects of risk management.

Environment and Safety Committee
~ Assists the Board of Directors in fulfilling its obligations and oversight responsibilities related to adherence to environmental laws and regulations and the safety of employees and the general public who may be impacted by BCRC's activities.

Human Resources, Governance and Nominating Committee
~ Assists the Board of Directors by fulfilling obligations relating to senior management human resource and compensation issues, ensuring that appropriate corporate governance policies and procedures are put in place, and to ensure that the membership of the Board is relevant to the obligations of BCRC.

Ad hoc special purpose committees are established as required.

Location

The offices of BCRC are located in Suite 400 – 221 West Esplanade, North Vancouver, British Columbia, V7M 3J3.

2.0 STRATEGIC CONTEXT

Mission

Establish an effective management system for the Revitalization Agreement between BCRC and CN while ensuring the efficient wind down and/or disposition of BCRC's remaining businesses, assets and non-railway related real estate.

Values

Integrity

~ Decisions made in a manner that is consistent, professional and fair.

Fiscal responsibility

~ Maximize return from the disposition of businesses, assets and non-railway related real estate.

Accountability

~ Ensure full reporting of activities to the shareholder.

Safety

~ Ensure a safe and healthy work environment.

Respect

~ Treat everyone in an honest, fair and respectful manner.

3.0 PLANNING CONTEXT AND KEY STRATEGIC ISSUES

Revised Mandate

BCRC has undergone a significant organizational transformation from being owner of the railway right-of-way and operator of the railway, to being owner of the railway right-of-way with responsibility for railway operations moving to the private sector. As a result of this transformation, BCRC has a revised mandate. The transformation process and revised mandate creates a challenge for both the Board and the management team in ensuring that the Shareholder's expectations are fully understood, adequately articulated and appropriately implemented. The Minister of Transportation, on behalf of the Shareholder, has provided clear direction to BCRC regarding its new mandate and an appropriate course of action required to meet that mandate through the Shareholder's Letter of Expectations.

Organizational Challenges

The Board, management team and retained staff, while substantially reduced from pre-transformation levels, have extensive organizational knowledge of both the previous operations of BCRC and the future expectations of the Shareholder. In essence, they share a corporate memory and provide much needed continuity.

With the transfer of the freight railway operations to CN, there is a much reduced employee level at BCRC which has created some capacity issues. The Investment Partnership with CN is a complex transaction that will continue to demand management attention over the period of the Service Plan. To date, management has focused on ensuring a smooth transition of the freight railway to the new operator. In addition, significant effort has been directed towards establishing appropriate and independent financial management and information technology systems previously provided by BC Rail Ltd. While minimal, the information technology support is adequate for the short term requirements of the organization. Strategic planning is also underway to prepare the remaining businesses, assets and non-railway related real estate for disposition and/or dissolution.

BCRC's new role as landlord to CN as tenant on the railway right-of-way means that an effective management system for the lease must be developed. As the time line to complete the bulk of the wind down and disposition processes is less than a year (to the end of 2005), a transition strategy for the residual entity must also be developed to ensure outstanding issues are dealt with and the on-going landlord-tenant relationship is effectively managed. This transition strategy will also address how residual issues will be dealt with by the Shareholder at the end of 2005. A shared services model with another Crown agency or line ministry will be explored as part of the development of the transition strategy.

Operating Environment

In order to fully deliver on the Shareholder's expectations in an effective and efficient manner, cooperation from other levels of government and stakeholders will be necessary. Many of the approvals required to complete all of the non-rail related real estate dispositions are beyond the control of BCRC. In addition, for some of the real estate scheduled for disposition, management must resolve outstanding issues such as environmental remediation, subdivision requirements, etc. Access to professional services such as real estate appraisals and land surveys are restricted by an increased demand for these services throughout British Columbia.

There are however, two factors which can assist BCRC to deliver on this aspect of its new mandate. One is that there is significant community support for the disposition of the residual businesses, assets and non-railway related real estate. The second factor is that the economy of British Columbia is stable and shows signs of continued improvement which in turn, will encourage private sector investment in the types of businesses and real estate currently slated for disposition. The investment opportunities provided through the disposition process could prove to be beneficial for many communities in British Columbia.

4.0 GOALS, STRATEGIES AND PERFORMANCE MEASURES

The BCRC/CN Investment Partnership has fundamentally changed the company's mandate and operating environment. Therefore, new goals, strategies and performance measures were developed to demonstrate a commitment to achieving *an effective management system for the Revitalization Agreement between BCRC and CN while ensuring the efficient wind down and/or disposition of BCRC's remaining businesses, assets and non-railway related real estate.*

Goal One

Ensure effective and efficient management of the Revitalization Agreement between BCRC and CN.

Strategies:

- ❑ Manage positive landlord-tenant relationship between BCRC and CN
- ❑ Refine management plan for Revitalization Agreement
- ❑ Transition Revitalization Agreement management system to the Shareholder

Performance Measures	**2005**	**2006**	**2007**
Progress in development of appropriate landlord-tenant relationship	*Protocol established to guide on-going relationship*	*Shareholder accountable*	*Shareholder accountable*
Management plan guiding Revitalization Agreement	*Management plan and guidelines completed*	*Shareholder accountable*	*Shareholder accountable*
Shareholder fully understands landlord-tenant relationship	*Report quarterly to Shareholder on landlord-tenant issues*	*Shareholder accountable*	*Shareholder accountable*

Goal Two:

Complete disposition activities for all remaining business units, assets and non-railway related real estate while maximizing the financial return to the shareholder where possible.

Strategies:

- ❑ Develop a strategic plan for business units, assets and non-railway related real estate to guide disposition
- ❑ Ensure all dispositions are properly supported by professional appraisals and other market benchmarks
- ❑ Ensure strong fiscal management and reporting

Performance Measures	**2005**	**2006**	**2007**
Strategic plans completed for each business unit, all assets and the real estate portfolio	*100%*	*Shareholder accountable*	*Shareholder accountable*
Percentage of business units, assets and real property disposed of within the disposal guidelines approved by the Board of Directors	*100%*	*Shareholder accountable*	*Shareholder accountable*
Net income outlook achieved	*$75.9 m*	*Shareholder accountable*	*Shareholder accountable*

5.0 ALIGNMENT WITH GOVERNMENT'S STRATEGIC PLAN

The British Columbia Railway Company Annual Service Plan 2005 to 2007, supports the British Columbia Government Strategic Plan 2004/05 – 2006/2007, specifically, *"Goal One: A Strong and Vibrant Economy"* which identifies the following objectives:

- A thriving private sector economy that creates high-paying job opportunities; and
- Responsible, accountable management of public resources and tax dollars.

In making the shift towards its new mandate, BCRC has developed a series of goals which, when achieved, will result in outcomes that should benefit the private sector economy in British Columbia. In addition, the focus on a strategic methodology to achieve the mandate will assist in ensuring responsible, accountable management of public resources and a defensible financial return to the shareholder and the tax payer.

6.0 *SUMMARY FINANCIAL OUTLOOK*

($ thousands)	2004 ESTIMATE	2005 BUDGET	2006 OUTLOOK	2007 OUTLOOK
Total Revenue	230.8	62.4	4.6	0.3
Operating Expenses	186.9	48.4	5.2	0.5
Amortization	31.3	12.4	7.8	6.7
Total Expenses	218.2	60.8	13.0	7.2
Operating Income	**12.6**	**1.6**	**(8.4)**	**(6.9)**
Financing income (costs)	(13.1)	1.7	3.6	4.3
Gain on disposal of assets	8.1	76.1	25.0	7.7
Write down of assets	(13.9)	N/A	N/A	N/A
Estimated gain on industrial freight transaction	195.9	N/A	N/A	N/A
Other	5.7	(3.5)	0	0
Net Income	**195.3**	**75.9**	**20.2**	**5.1**
Capital Expenditures	53.9	21.7	5.8	0

Notes on Revenues and Expenses

The 2004 results are the estimated results as of January 27, 2005, and are subject to change pending completion of the year end close process, external audit and approval by BCRC's Board of Directors. In BCRC's 2004 budget, it was assumed that the transaction with CN would close on March 31, 2004. As a result, the 2004 budget included the operating results of the industrial freight railway only up to this date. The 2004 estimated results noted above include the operating results of the industrial freight railway up to the date of the conclusion of the transaction with CN (July 14, 2004). The gain on the industrial freight railway transaction is still an estimate at this time until the external audit is complete and the audited financial statements have been approved by the Board of Directors in March 2005. The 2005 budget includes the results of

Vancouver Wharves, BCR Properties, BCR Port Subdivision and BCRC for the entire year.

Amortization expense in the 2005 budget includes $6.7 million for assets leased to CN which have been treated as a capital lease.

BCRC repaid all of its outstanding debt with the Province with the proceeds from the CN transaction in July 2004. The debt was repaid at its fair market value of $509.0 million. The 2004 budget assumed that BCRC would complete a debt defeasance and the estimated cost of this was included in the budget for financing costs. Instead, BCRC settled its debt with the Province and the difference between fair market value and book value of $40.8 million has been recorded through equity as required by related party transaction accounting rules. Financing income arises from the investment of excess cash being retained for corporate or operating purposes.

Key Assumptions

The budget assumes that Vancouver Wharves and BCR Port Subdivision will be sold on December 31, 2005. It is possible that these transactions may take place at some other point, either during 2005 or after 2005. Due to the uncertainty of timing of these transactions and that there is no current formal disposition plan these entities have been treated as continuing operations in the budget. It is assumed that the current environmental accrual for Vancouver Wharves is paid in 2005.

BCR Captive Insurance Co. will cease to provide insurance to BCRC and its subsidiaries as of September 30, 2005, which coincides with the termination of the existing 3 year insurance policy. Risk Management Branch, Ministry of Finance, will arrange insurance for the remaining assets after this point. BCR Captive will be wound up as soon as possible after September 2005. However, outstanding claims and litigation may delay its wind up for several years.

BCR Properties Ltd. will continue with its mandate to dispose of all of its property holdings by the end of 2006.

BCRC will have a full administration office during 2005. After 2005, the remaining functions and responsibilities of BCRC will be amalgamated into government. No wage or salary increases have been budgeted.

Forecast Risks and Sensitivities

Proceeds on the disposition of Vancouver Wharves, the Port Subdivision or the non-railway related real estate portfolio could be greater or less than what is included in the budget impacting the gain/loss on sales.

There is some risk associated with the Vancouver Wharves operations (i.e., ability to achieve their operating budget) but the Board has and will continue to, carefully monitor this situation.